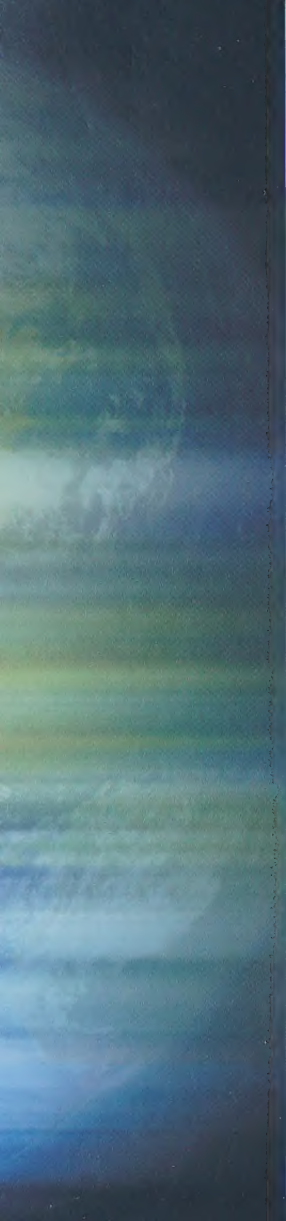
Environment Focus Innovation

ZCL Composites Inc Annual Report 2005

ZCL COMPOSITES INC.



Who we Are

What we Do

ZCL is Canada's leading designer, manufacturer and supplier of economical and environmentally-safe liquid storage systems. Our growth over the past 17 years is attributed to our ability to innovate and leverage our core expertise and technology to meet industry needs for fiberglass tanks and other storage systems. ZCL and its subsidiaries provide proactive, comprehensive and cost-effective liquid storage solutions. Our customers have embraced our developments and inspire us to continue to strive for industry leadership.

Mission Statement

To provide global solutions for the economical and environmentally-safe storage of petroleum products and other liquids.

Canada's 50 Best Managed Companies

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Focused on Growth & Innovation

The Company has led the way in innovative fiberglass tank technology, from the Underwriters' Laboratories of Canada (ULC) listed single wall storage tank in 1988, to the development and introduction of the first double wall tank manufactured in Canada. Our Prezerver® system and other product innovations, such as the Protektor® aboveground tank, have a high level of industry acceptance. Using the same proven technology and manufacturing expertise, a number of new products have been recently successfully introduced into several market sectors.

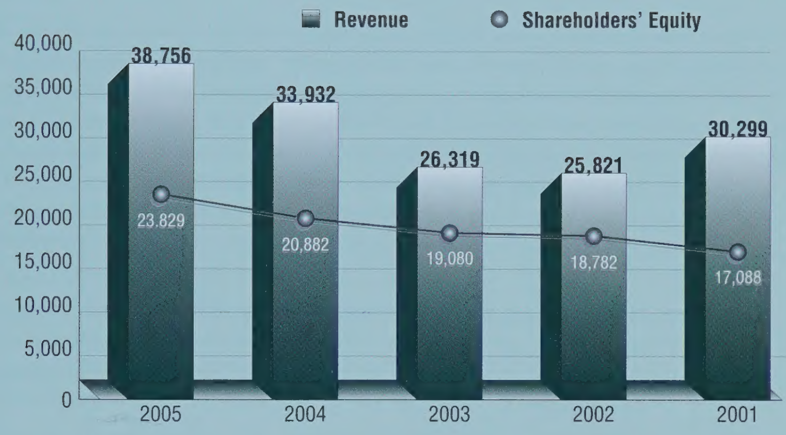
The Company has demonstrated innovative leadership and has kept pace with the changing needs of the marketplace with expanding product lines for many applications, including double wall tank upgrade systems and aboveground products to compete in markets traditionally served only by steel tanks. Our current focus is the development and marketing of our tank lining technologies, as well as other new products. The Company is working with customers and suppliers to develop new lining materials and processes in order to deliver a product with superior quality and performance, along with inherently safe installation techniques.

"ZCL continues to innovate with expanding product lines for many applications and industries, including double wall tank upgrade systems..."

Financial Highlights

(in thousands of dollars, except share information)	2005 $	2004 $	2003 $	2002 $	2001 $
Consolidated Statements of Income					
Revenue	38,756	33,932	26,319	25,821	30,299
Provision for impairment of agreement receivable, restructuring and license litigation costs *[note 1]*	—	880	—	98	936
Net income *[note 2]*	3,480	1,952	756	1,836	1,534
Basic earnings per share *[note 2]*	0.20	0.11	0.02	0.11	0.09
Diluted earnings per share *[note 2]*	0.18	0.11	0.02	0.11	0.09
Consolidated Statements of Retained Earnings (Deficit)					
Convertible subordinated debenture costs, net of tax *[note 3]*	—	—	(461)	(815)	(718)
Dividends	(1,051)	—	—	—	—
Deficit elimination *[note 4]*	—	9,043	—	—	—
Retained earnings (deficit), end of the year	4,381	1,952	(9,043)	(8,976)	(9,997)
Consolidated Statements of Cash Flows					
Cash flows from operating activities	2,286	6,101	3,435	2,464	5,134
Purchase of property, plant and equipment	432	581	455	155	528
Consolidated Balance Sheets					
Working capital *[note 5]*	12,898	10,099	8,669	7,863	4,827
Total assets	32,624	26,467	28,014	24,489	26,080
Long-term debt (including current portion)	—	—	4,643	1,912	2,634
Shareholders' equity *[note 6]*	23,829	20,882	19,080	18,782	17,088
Common shares, end of the year	17,943,919	17,511,320	17,716,920	9,295,866	9,295,866

Management considers the above earnings and other measures to be meaningful indicators of the financial position, results of operations and cash flows of the Company. Readers are cautioned that some of these measures may not have standardized meanings prescribed by Canadian generally accepted accounting principles, and are therefore not readily comparable to, and may be different than the calculations of, similar measures provided by other corporations.



Note 1 – In 2004, a provision for impairment of the full amount of an agreement receivable from ZCL Enviro Systems, Inc. was recorded. In 2002 and 2001, restructuring and license litigation costs were legal, occupancy and other costs related to the litigation with Xerxes Corporation in the USA, the review of operations and dispute with ZCL-USA, Inc., the shutdown of the Belleville, Ontario plant, and management restructuring and termination. These costs were not considered to be part of the ongoing operations and not expected to recur in the future. They were separately disclosed in the Consolidated Statements of Income in the consolidated financial statements.

Note 2 – Goodwill charges of $161,000 were deducted in 2001 before the change in accounting policy in 2002 whereby goodwill is not amortized.

Note 3 – Convertible subordinated debenture costs, net of tax, were charged directly to retained earnings and deducted for purposes of determination of the basic and diluted per share computations.

Note 4 – At the Annual General and Special Meeting of Shareholders on August 18, 2003, the shareholders approved the reduction of the stated capital of the Company and elimination of the accumulated deficit.

Note 5 – Working capital is calculated as current assets less current liabilities recorded on the consolidated balance sheets.

Note 6 – Shareholders' equity included the equity portion of the convertible subordinated debenture prior to repayment in September 2002.

Message to Shareholders

Former ZCL Chairman of Board Gilles Voyer (left) and current President and Chief Executive Officer Ven Côté (right), September 1995

We celebrate our tenth year of listing on the Toronto Stock Exchange. 10 years on the TSX

As we celebrate our tenth year of listing on the Toronto Stock Exchange, our vision remains unchanged: to be the leading global provider of environmentally-friendly liquid storage solutions. An important element of this vision is to also provide superior returns to our shareholders. To realize our vision, we must maintain our position in our traditional markets in the Canadian marketplace, and pursue growth opportunities in related products and markets.

We remain committed to this strategy of profitable growth. We targeted annual growth in revenue of 15% to 20%, along with a corresponding increase in income. We came very close to reaching this goal in fiscal 2005 and are now poised and confident that we can meet this target in 2006.

2005 was a very successful and another record setting year for ZCL. We are pleased to report revenue for the year ended March 31, 2005 increased by 14.2% to a record \$38.8 million. Net income increased by \$1.5 million for the year, to a record \$3.5 million, basic earnings per share increased by \$0.09 to \$0.20 and diluted earnings per share increased to \$0.18.

Revenue in fiscal 2005 was higher than 2004 in each quarter, except for the first quarter where activity started slowly but picked up during the quarter. The second, third and fourth quarters of 2005 once again established new record levels. Activity in the downstream and upstream sectors of the petroleum industry, as well as other traditional markets, continued to be strong throughout 2005. Products we introduced in recent years – home heating oil tanks, Protektor® and Pinnacle™ oilfield tanks, filament wound pressure vessels, and custom storage and lining systems – as well as new steel products with the acquisition of the business assets of Durex Steel & Alloy Industries Ltd. ("Durex") continue to gain market acceptance and contribute to our revenue.

We have targeted the aboveground tank and tank lining markets for the next phase of our growth. To this end, we have made some great strides during the past year.

The acquisition of the business assets of Durex in May 2004 allows us to access the aboveground retail storage market which has eluded us until now. Our tank manufacturing and lining operations are now expanded, and a full line of products, including steel and fiberglass-lined steel, are offered to existing alliance customers as well as to new customers.

We began field testing of our lining system in November 2004 and final testing is scheduled to be completed in the early part of fiscal 2006. Our lining process, now renamed the "Lifeliner", upgrades a single wall tank "in-situ" with a three-dimensional laminate using patented materials combined with a proprietary state-of-the-art curing system. The system also allows storage of new fuels, including the new

We are pleased to report revenue for the year ended March 31, 2005 increased by 14.2% to a record $38.8 million.

ethanol and other blends now being legislated in certain parts of Canada and USA. We estimate that the potential annual lining market in North America is in excess of $300 million. With the anticipated listing by Underwriters' Laboratories of Canada (ULC) and Underwriters' Laboratories (UL), we expect that this new product will add to our revenue in 2006. We will cautiously introduce lining systems to the marketplace, and our lining program will be ramped up as we gain field experience and train qualified applicators in all aspects of this new system.

We also received UL approval for our home heating oil tank, another very promising product that we are now introducing to the USA market. The North American home heating oil market represents an annual potential of 500,000 to 600,000 units or $400 to $500 million. Our objective is to significantly grow our market share over the next five years.

Just after year-end, we completed the purchase of 100% of the shares of Triple M Fiberglass Mfg. Ltd. ("Triple M"), a manufacturer of fiberglass aboveground and underground tanks, vessels, pipe and other custom environmental products, located in Edmonton, Alberta. Triple M's specialized products and unique manufacturing expertise further enhance our product line and open new markets for us.

As we have highlighted before, our customers are the foundation of our success. This past year, we were privileged to sign or renew long-term supply agreements with several major customers. Two more were announced subsequent to March 31, 2005. These companies have indicated their faith in ZCL and our products.

In January 2005, we were once again honoured as one of Canada's 50 Best Managed Companies. This prestigious award is yet another endorsement of our Company and the people behind our success. Our team is devoted to quality products, constantly setting a higher standard for economical, environmentally-safe and long-lasting liquid storage technology.

Over the course of the year, our share price traded between a low of $1.00 and a high of $3.82. Our performance has attracted new shareholders and the attention of some institutional investors, thus creating more liquidity for our shares.

I am sincerely grateful for the valuable support of our customers, shareholders and directors, and for the outstanding efforts of our team of now 235 employees across the country and abroad. People really do make a difference – they certainly do at ZCL. Your continued support and dedication will drive future growth and build value for our shareholders.

Venence G. Côté
President and Chief Executive Officer

May 2005

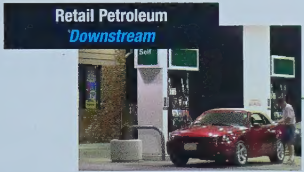
Safe, Proven, Time-tested

As communities, industries, businesses and governments have been increasingly aware of the need for safe, environmentally-friendly storage of many liquids, ZCL's corrosion-resistant, lightweight and structurally-strong tanks have proven to be the product of choice for many applications. Most of Canada's largest oil companies and petroleum marketers rely on our systems for the safe underground and aboveground storage of their petroleum products and other hazardous liquids. In the past 17 years alone, more than 30,000 ZCL tanks have been installed and our tanks have never had a single leak attributed to internal or external corrosion. A clear indication that durable, corrosion-resistant fiberglass tanks are the tank of choice in the underground retail petroleum industry, is that an estimated 90 percent of all purchases are ZCL fiberglass products.

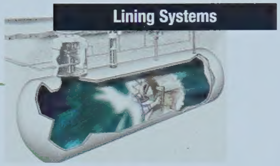
In the past 17 years alone, more than 30,000 ZCL tanks have been installed for the storage of liquid products...

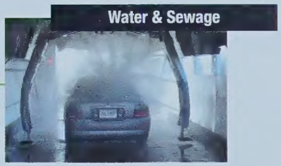
Liquid Storage Markets

Our customers are the foundation of our success. We continue to innovate with expanding product lines of fiberglass tanks and accessories for the safe storage of petroleum products, hazardous liquids, sewage and water.



Core Markets





Emerging Markets

Products & Services

ZCL manufactures and distributes liquid storage systems including fiberglass underground and aboveground storage tanks and related products and accessories. We market ULC-listed underground storage tanks to the retail petroleum industry under the trademarks Prezerver® and Greentank®. The Company also markets, under the trade name Prezerver® System, a complete fuel storage system that carries a $2 million insurance-backed warranty against pollution.

ZCL manufactures and supplies aboveground tanks and pressure vessels for the upstream oil and gas industry. These tanks are designed for the safe storage of brine and other hazardous liquids and are marketed under the trademarks Protektor® and Pinnacle™.

The Company also produces secondary containment products, using a three-dimensional tank lining system, under the trademark Everlast™. Our secondary containment steel tanks are sold under the Duragreen® trademark.

The Lifeliner System™, researched and developed by ZCL, is a unique internal fiberglass system that upgrades any in-situ underground single wall storage tank (of any condition) to a secondary containment system with monitoring capabilities. The growing demand for this type of system is driven by ageing and leaking tanks, as well as the emergence of new fuels and additives.

Another product innovation is the Company's tank for the safe storage of home heating oil. Our fiberglass, aboveground, stationary home heating oil tank is marketed under the trade name The Safer Tank™.

Central to many of our products is the Parabeam® 3D glass fabric. Its unique properties make Parabeam® the ideal solution wherever a lightweight and rigid structure is required. Through its subsidiary Parabeam Industries BV, Parabeam® is manufactured for numerous applications in the corrosion, marine, transport and building and construction industries.



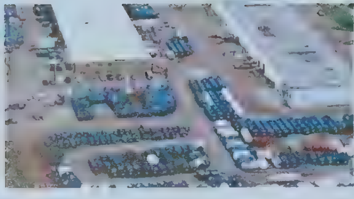
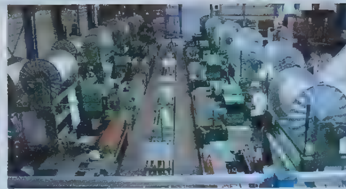

Over the years, ZCL's product line has expanded to meet customers' needs. In addition to single wall and double wall tanks, we now offer multi-compartment tanks, oil-water separators, and filament wound pressure vessels. In the growing water and sewage treatment markets, the flexible design options of ZCL tanks make them very adaptable. Our tanks are easy to install in a wide variety of underground storage applications, including potable water, car wash effluent, fire-protection, storm water runoff and domestic sewage. We also offer a full line of custom, corrosion-resistant, fiberglass products for above-ground applications. Products include storage and process tanks, fiberglass pipe and fittings and custom-fabricated vessels and equipment for use in the industrial, chemical, oil and gas and government sectors.

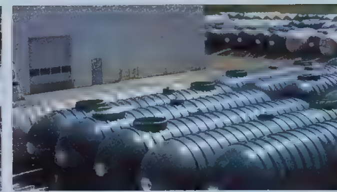
The ZCL Everlast division has seized the opportunity to expand the Company's product line in both the upstream and downstream markets. We now offer a full line of fiberglass, steel and fiberglass-lined steel tank products.

The Company continues to deliver a complete liquid storage solution to the marketplace through our association with major Canadian distributors of liquid handling equipment. Our tanks and products have become the standard for the safe storage of petroleum products in Canada.

the safer tank™

Safe and durable, fiberglass tanks have become the #1 choice for environmentally-safe storage of petroleum products.



Manufacturing Facilities

ZCL has over 235 skilled employees in seven manufacturing facilities.

Since ZCL's establishment in 1987, our vision has been to be the leading global provider of economical and environmentally-friendly liquid storage solutions. The initial focus was the manufacture and sale of fiberglass reinforced plastic (FRP) underground storage tanks for use in the downstream petroleum industry, primarily for storage of gasoline at retail outlets. We now also supply the upstream oil and gas sector, as well as many other industries, with both underground and aboveground storage systems. Recently renewed long term alliance agreements with major and independent oil companies ensure future demand for ZCL's products.

We have over 235 skilled employees in seven manufacturing facilities across Canada and in The Netherlands. The Company has strategically located plants to serve its customers:

- Edmonton, Alberta and Drummondville, Quebec manufacture underground and aboveground fiberglass tanks;
- Waverley, Nova Scotia produces fiberglass home heating oil tanks;
- Nisku, Alberta and Edmonton manufacture aboveground primary storage and secondary containment steel and fiberglass-lined steel tanks;
- Helmond, The Netherlands manufactures the three dimensional Parabeam® fabric used in numerous industrial applications;
- With the acquisition of Triple M Fiberglass Mfg. Ltd., this Edmonton plant manufactures fiberglass underground and aboveground tanks, vessels, piping and other environmental products.


Snacks
Clearance
13'-4"
Self
ICE

Management's Discussion and Analysis

May 20, 2005

The following discussion and analysis should be read in conjunction with the audited consolidated financial statements of the Company for the years ended March 31, 2005 and 2004, and the notes relating thereto, as well as the Message to Shareholders and other management discussion included in this Annual Report. Financial statements are prepared in accordance with Canadian generally accepted accounting principles, and all amounts are in Canadian dollars unless otherwise indicated.

This report includes forward-looking statements that are based on current expectations and are subject to risks and uncertainties. Many internal and external factors may cause actual results to differ materially, including, but not limited to, those outlined in Risks and Uncertainties below. The Company disclaims any intention or obligation to update or revise any such forward-looking statements, whether as a result of new information, future events, or otherwise.

Overall Performance

The Company operates in one reportable segment, which is the manufacture and distribution of liquid storage systems including fiberglass underground and above-ground storage tanks and related products and accessories. Historically, the second and third fiscal quarters have the highest levels of activity, corresponding to the seasonality of the installation of underground liquid storage systems in Canada.

Revenue in 2005 increased by 14.2% to a record $38.8 million, from $33.9 million in 2004. Net income increased by $1.5 million, to a record $3.5 million from $2.0 million in 2004. Basic earnings per share increased by $0.09, to $0.20 from $0.11 in 2004, and diluted earnings per share increased to $0.18 from $0.11 in 2004.

Revenue in 2005 was higher than 2004 in each quarter, except for the first quarter where activity started slowly but picked up during the quarter. The second, third and fourth quarters of 2005 once again established new record levels.

Activity in the downstream and upstream sectors of the petroleum industry, as well as other traditional markets, continued to be strong throughout 2005. Products introduced in recent years – home heating oil tanks, Protektor® and Pinnacle™ oilfield tanks, filament wound pressure vessels, and custom storage and lining systems – as well as new steel products with the acquisition of the business assets of Durex Steel & Alloy Industries Ltd. ("Durex"), continue to gain market acceptance and contribute to revenue.

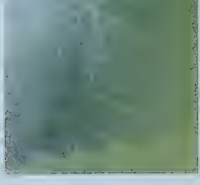
The increase in net income in 2005 was due largely to the higher revenue. In addition, amortization expense decreased from 2004 as certain deferred costs related to past start-up operations and acquisitions were fully amortized during the year, and financing charges were lower as a result of the repayment of long-term debt in 2004. Net income in 2004 was also reduced by $880,000 ($580,000 after tax, or $0.03 per share) due to the provision for impairment of the agreement receivable from ZCL Enviro Systems, Inc. ("Enviro").

Cash flows from operating activities decreased by $3.8 million, to $2.3 million in 2005 from $6.1 million in 2004, due to the timing of sales (high sales late in the fourth quarter with the resulting high level of accounts receivable at March 31, 2005) and the build-up of inventories this year. Cash used in financing activities decreased by $4.2 million, to $640,000 this year from $4.8 million in 2004. In 2005, dividends of $1.1 million were paid and common shares were issued for cash of $411,000 upon the exercise of share options and warrants. In 2004, long-term debt of $4.6 million was repaid and common shares were repurchased for $189,000 under the normal course issuer bid. Cash used in investing activities increased by $1.4 million, to $2.1 million this year from $722,000 in 2004, largely as a result of the purchase of the business assets of Durex for cash of $1.2 million.

In December 2004, a portion of the Company's manufacturing plant in Waverley, Nova Scotia was destroyed in an electrical fire. This facility is used largely to produce home heating oil tank products. All damaged property, equipment and inventories have been repaired or replaced. It is anticipated that insurance proceeds from the Company's insurers (subject to the $25,000 deductible under the insurance policy) will cover all damages. Accounts receivable at March 31, 2005 included $590,000 related to the insurance claim, of which $250,000 was collected subsequent to year-end. Manufacturing has resumed and the plant was fully restored with no major disruptions to production or sales as a result of the fire.

A current focus of the Company is final testing and marketing of tank lining technologies. New lining materials and processes have been developed in conjunction with customers and suppliers to deliver a product with superior quality and performance and inherently safe installation techniques. Product development costs of $518,000 were deferred during the year (2004 - $141,000). Final field testing is scheduled to be completed in the early part of fiscal 2006. With the anticipated listing by Underwriters' Laboratories of Canada ("ULC") and Underwriters' Laboratories ("UL"), this new product is expected to add to revenue in fiscal 2006. Lining systems will be cautiously introduced to the marketplace and the lining program will be ramped up as field experience is gained and qualified applicators are trained in all aspects of this new system.

Another focus is the marketing of home heating oil tanks. Following the UL approval of these tanks for the USA market, marketing and sales activities commenced in the New England states during the latter part of the year. Heating or furnace oil is used for heating in about 8 million households in North America, largely Eastern Canada and North-Eastern USA. A growing concern is the environmental and liability problems resulting from leaking tanks, and the Company's fiberglass products offer a new level of security for home owners, insurance companies and lenders.



Selected Annual Information

(in thousands of dollars, except per share amounts)	2005 $	2004 $	2003 $
Consolidated Statements of Income			
Revenue	**38,756**	33,932	26,319
Net income	**3,480**	1,952	756
Basic earnings per share	**0.20**	0.11	0.02
Diluted earnings per share	**0.18**	0.11	0.02
Consolidated Balance Sheets			
Total assets	**32,624**	26,467	28,014
Long-term debt (excluding current portion)	–	–	3,929
Cash Dividends Declared			
Total	**1,051**	–	–
Per common share	**0.06**	–	–

In fiscal 2002, various upgrade and new installation programs in both the upstream and downstream sectors of the petroleum industry were deferred because of economic and political uncertainty, low commodity prices and merger and acquisition activity. This reduced level of activity in the petroleum industry, and many other industry sectors, continued into fiscal 2003, as economic and political uncertainty persisted. In the latter part of fiscal 2003 and throughout 2004 and 2005, revenue increased as a result of strong activity in the downstream and upstream sectors of the petroleum industry, the growing market acceptance of new products introduced by the Company in recent years, and the acquisitions of Mocoat Services Incorporated ("Mocoat") in May 2002, Parabeam Industries BV ("Parabeam") in September 2002 and Durex in May 2004.

Net income was negatively impacted in 2003 by costs incurred to integrate Mocoat and Parabeam into the overall liquid storage business, and in 2004 by the provision for impairment of the agreement receivable from Enviro. Amortization of deferred costs and intangible assets increased in 2003 and 2004 with the acquisitions of Mocoat and Parabeam, as well as the assets of ZCL-USA, Inc. purchased in 2002. Amortization decreased during 2005, as certain of these costs were fully amortized. Financing charges also decreased in 2005 with the repayment of the long-term debt in November 2003.

Total assets increased in 2003 with the acquisitions of Mocoat and Parabeam. During 2003, common shares and warrants were issued for $7.0 million and long-term debt was issued for $5.0 million; these proceeds were used to repay a subordinated convertible debenture as well as all previous long-term debt. During 2004, all remaining long-term debt was repaid. In 2005, assets increased due to the acquisition of the assets of Durex, as well as higher working capital (increased accounts receivable and inventories) required for the elevated level of operations.

Results of Operation

Year Ended March 31, 2005 Compared to the Year Ended March 31, 2004

Revenue

Revenue was $38.8 million in 2005 compared to $33.9 million in 2004, an increase of over $4.8 million or 14.2%. Revenue increased due to the sustained strength of the downstream and upstream sectors of the petroleum industry and other traditional markets, and the Company's expanding line of products. These products, both new products introduced in recent years and products added with the acquisitions of Mocoat, Parabeam and Durex, although relatively new to their markets and not as significant as the major products, continue to gain market acceptance and contribute to revenue.

Revenue less manufacturing and selling costs

Revenue less manufacturing and selling costs increased to $9.1 million (23.4% of revenue) from $8.0 million in 2004 (23.5% of revenue). The increase is a result of the higher revenue in 2005. The development of the tank lining technologies is in the final stages of testing, and costs which meet the criteria established by the Canadian Institute of Chartered Accountants ("CICA") have been deferred.

Manufacturing and selling costs include direct materials and labour, variable and fixed manufacturing overhead, and marketing and selling expenses, and exclude amortization, general and administration, and financing charges. While overall margins have decreased slightly, mainly as a result of increased raw material costs, ongoing margins are expected to be maintained through selling price increases and production improvements. Manufacturing overhead and marketing and selling expenses have generally been maintained at similar levels as last year, but certain higher expenses were incurred to support the higher operations and sales activity.

The Company has an ongoing continuous improvement program aimed at reducing costs and maximizing operational efficiency. The initial ISO certification of two of the Company's production facilities, and the subsequent update to ISO 9001:2000, are part of this continuing program.

Amortization

Amortization decreased by $210,000 to $1.8 million for the year, from $2.0 million in 2004.

Amortization had increased during the last two years as a result of deferred costs and intangible assets added with the acquisitions of Mocoat and Parabeam in 2003, and the assets of ZCL-USA, Inc. in 2002. These were key strategic acquisitions related to the tank lining products, and to the proprietary three-dimensional glass fabric that is an integral part of the Company's manufactured and lining products. The overall level of amortization decreased in the latter part of 2005, as certain of these costs were fully amortized.

Additional lining development costs were deferred this year and final testing is scheduled for the early part of fiscal 2006. These costs will be amortized in fiscal 2006 upon the commercial production of the lining products.

General and administration

General and administration expenses increased by $156,000, from $1.9 million in 2004 to $2.0 million in 2005, but decreased as a percentage of revenue from 5.5% in 2004 to 5.2% in 2005.

Over the past several years, the overall level of general and administration expenses have been maintained or reduced through restructuring and cost reduction efforts. These expenses will, however, increase as the Company grows and systems and procedures are put in place, and associated professional fees and other costs are incurred, relating to the requirements of current corporate governance.

Provision for impairment of agreement receivable

During 2004, a provision for impairment of the full amount of the agreement receivable from Enviro of $880,000 was recorded. As described in note 12 to the consolidated financial statements, the amounts and timing of future repayment, and the fair value of underlying security, net of expected costs of realization, could not be estimated with reasonable reliability. Since that time, actions continue to be pursued to collect the amount receivable or otherwise realize upon security, but no additional recoveries have been received.

Financing charges

Financing charges were $73,000, down from $370,000 in 2004. As described in note 13 to the consolidated financial statements, financing charges represent interest on short-term indebtedness, including bank fees and other charges, and foreign exchange losses, as well as interest on long-term debt and amortization of deferred finance charges in 2004.

During fiscal 2004, all long-term debt was repaid, and the related deferred finance costs were written-off. Interest on short-term indebtedness was higher this year with some utilization of the bank lines of credit (bank indebtedness) during the year. Foreign exchange losses of $22,000 (2004 – $12,000) were related to transactions denominated in foreign currencies and the translation of the financial statements of Parabeam.

Income taxes

The Company's effective tax rate was 33.4% in 2005 as compared to 32.1% in 2004. The Company's overall statutory income tax rate is approximately the same as last year. Income taxes were higher in 2005 due to additional non-deductible expenses in 2005 (largely stock-based compensation expense which increased to $98,000 from $10,000 last year) and the recovery of prior years' taxes of $145,000 in 2004 which did not occur in 2005. In 2005, a tax benefit of $68,000 was realized due to losses not previously recognized for accounting purposes.

The Company was in a taxable position this year. Future income taxes relate primarily to the utilization of losses of prior years for tax purposes, and differences between financial reporting and tax bases of assets and liabilities. The majority of tax losses of prior years have been utilized, and current future tax assets largely represent the remaining tax losses that are available and anticipated to be utilized over the next year. The Company has accumulated losses for tax purposes which may be carried forward to reduce taxable income in future years as described in note 14 to the consolidated financial statements. The potential income tax benefit associated with these losses has been recognized for accounting purposes.

Net income and earnings per share

Net income increased by $1.5 million, to a record $3.5 million from $2.0 million in 2004. Basic earnings per share increased by $0.09, to $0.20 from $0.11 in 2004, and diluted earnings per share increased to $0.18 from $0.11 in 2004.

The weighted-average number of common shares for basic earnings per share increased to 17,686,512 as compared to 17,640,106 in 2004, as a result of the share options and warrants exercised during the year.

With the increased market share price, the effect for 2005 of dilutive share options and warrants was 1,595,431 (2004 – 48,041). Two-thirds of the warrants vested this year, with the first performance threshold of $1.90 per common share reached in the first quarter, and the second threshold of $2.85 in the third quarter. In 2005, the warrants that had not vested were not included in the calculation of diluted shares. In 2004, certain stock options were not included as their exercise prices exceeded the average market share price, and the warrants were not included as the market share price was below the performance vesting thresholds.

Summary of Quarterly Results

Quarterly Results

(in thousands of dollars, except per share amounts)	Q1 Jun 30	Q2 Sep 30	Q3 Dec 31	Q4 Mar 31	Year
2005					
Revenue	6,308	11,020	11,056	10,372	38,756
Net income	72	1,229	1,028	1,151	3,480
Basic earnings per share	$0.00	$0.07	$0.06	$0.07	$0.20
Diluted earnings per share	$0.00	$0.07	$0.05	$0.06	$0.18
2004					
Revenue	7,409	7,896	10,726	7,901	33,932
Net income	236	97	1,134	485	1,952
Basic earnings per share	$0.01	$0.01	$0.06	$0.03	$0.11
Diluted earnings per share	$0.01	$0.01	$0.06	$0.03	$0.11

Historically, the second and third fiscal quarters have the highest levels of activity, corresponding to the seasonality of the installation of underground liquid storage systems in Canada. This seasonality is expected to continue, but may diminish as the Company expands its product lines into new markets that have different seasonality or that are less influenced by the effect of weather in the timing of installation.

Revenue in 2005 was higher than 2004 in each quarter, except for the first quarter where activity started slowly but picked up during the quarter. The second, third and fourth quarters of 2005 once again established new record levels.

Liquidity and Capital Resources

The Company expects that cash flow from operations, current credit facilities and other potential capital resources will allow the implementation of growth programs, including development of new products and support of the overall growth of operations, and other expected financial requirements. At March 31, 2005, the Company had available operating lines of credit of $10,250,000 provided by a chartered bank that were not utilized.

In April 2005, the Company announced the acquisition of 100% of the shares of Triple M Fiberglass Mfg. Ltd. ("Triple M") for $1.9 million, subject to final adjustments, paid in cash on closing. In the event that other acquisitions are identified that are in the best interests of the Company, and meet strategic objectives, cash may be raised through the issue of additional debt and shares.

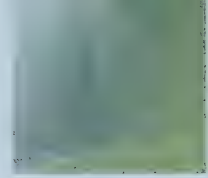
Working capital (current assets less current liabilities) increased by $2.8 million during the year to $12.9 million, as current assets increased by $5.9 million to $20.6 million at March 31, 2005, and current liabilities increased by $3.1 million to $7.7 million. These increases reflect the profitable and elevated level of operations during the year.

At March 31, 2005, accounts receivable increased by $4.9 million or 77% to $11.3 million, inventories increased by $1.6 million or 28% to $7.1 million, accounts payable and accrued liabilities increased by $1.8 million or 40% to $6.3 million, and income taxes payable increased by $1.3 million to $1.3 million. Accounts receivable and accounts payable and accrued liabilities reflect the increased fourth quarter activity this year. Accounts receivable at March 31, 2005 also included $590,000 with respect to the insurance claim related to the Waverley plant fire, of which $250,000 was collected subsequent to year-end. Inventories have been increased to meet the continuing higher level of activity. Income taxes payable increased as a result of the current tax provision for the year and because income tax instalments were not required during the year.

The Company deals largely with major oil and gas companies in Canada, performs ongoing credit evaluations and maintains allowances for potential doubtful accounts. No one customer generally makes up more than 10% of revenue, but at a particular point in time, depending on the timing of sales, there may be higher proportionate exposure in accounts receivable. At March 31, 2005, two customers accounted for 22% (2004 – two customers, 26%) of accounts receivable.

During 2004, a provision of $880,000 was recorded for the impairment of the agreement receivable from Enviro. Actions continue to be pursued to collect the amount receivable and any collections will have a positive impact on income and cash.

Shareholders' equity increased to $23.8 million, as a result of net income ($3.5 million), share options and warrants exercised (net $411,000), and stock-based compensation expense credited to contributed surplus ($107,000), less dividends paid ($1.1 million), during the year. At the Annual General and Special Meeting of Shareholders on August 18, 2003, shareholders passed a special resolution to eliminate the deficit at March 31, 2003 and reduce the stated capital of the Company. Accordingly, in the second quarter of 2004, contributed surplus was reduced by $745,000, share capital by $8.3 million, and accumulated deficit by $9.0 million.



Cash Flows

Cash flows from operating activities decreased by $3.8 million, to $2.3 million this year from $6.1 million in 2004. This decrease was primarily due to the large increase in accounts receivable (high level of sales late in the year) and build-up of inventories this year.

Cash used in financing activities decreased by $4.2 million, to $640,000 this year from $4.8 million in 2004. In 2005, dividends of $1.1 million were paid and common shares were issued for cash of $411,000 upon the exercise of share options and warrants. In 2004, long-term debt of $4.6 million was repaid and $189,000 of common shares were repurchased under the normal course issuer bid ("NCIB").

In August 2004, the Toronto Stock Exchange ("TSX") accepted notice of a normal course issuer bid ("2004 NCIB") filed by the Company. For the twelve-month period commencing August 19, 2004 and ending August 18, 2005, the Company may purchase on the TSX up to a maximum of 875,566 common shares, being approximately 5% of the issued and outstanding common shares. The actual number and timing of any purchases will be determined by the Company, and the price for any such shares will be the market price at the time. The Company believes that, from time to time, its common shares have been trading at a price range which does not adequately reflect their value in relation to the assets, business and future prospects. No shares have been purchased pursuant to the 2004 NCIB. The normal course issuer bid filed by the Company in July 2003 ("2003 NCIB") expired on July 9, 2004. In fiscal 2004, 222,000 common shares were repurchased for cancellation under the 2003 NCIB.

Summary of Cash Flows

Years ended March 31 (in thousands of dollars)	2005 $	2004 $
Operating activities	**2,286**	6,101
Financing activities	**(640)**	(4,832)
Investing activities	**(2,143)**	(722)
Increase (decrease) in cash	**(497)**	547
Cash, beginning of the year	**1,880**	1,333
Cash, end of the year	**1,383**	1,880

Cash used in investing activities increased by $1.4 million, to $2.1 million this year from $722,000 in 2004. The business assets of Durex were purchased for cash of $1.2 million in the first quarter this year. Property, plant and equipment additions in 2005 were $432,000 (2004 - $581,000). These additions related largely to equipment purchased to increase production capacity and efficiency, and the upgrade of computer equipment. Development costs of $518,000 (2004 - $141,000), related to the development of lining materials and processes, were deferred.

Contractual Obligations

Payments Due by Fiscal Year	2006	2007-2008	2009-2010	2011-2014	Total
	$	$	$	$	$
Long-term debt	–	–	–	–	–
License agreements	467	812	245		1 524
Operating leases	407	581	348	329	1,665
Total contractual obligations	874	1,393	593	329	3,189

The Company finances certain activities and requirements through license arrangements and operating leases. The above contract obligations exclude ongoing purchase commitments in the normal course of business; the Company has no long-term purchase commitments relating to operations or capital expenditures. In 2004, all long-term debt was repaid.

The Company has entered into long-term license agreements which expire between October 2006 and December 2008. These agreements give the Company rights to manufacture and sell products in certain geographic areas utilizing the licensors' technology. As described in the table above and note 8 to the consolidated financial statements, the undiscounted minimum royalty payments under these license agreements amounted to $1.5 million at March 31, 2005.

The Company leases certain of its premises and automotive and office equipment under long-term operating lease arrangements. As described in the table above and note 8 to the consolidated financial statements, the undiscounted minimum lease payments amounted to $1.7 million at March 31, 2005.

Government grants included in long-term liabilities on the balance sheet relate to government assistance received in prior years with respect to the purchase of property, plant and equipment. The Company has no obligation to repay the amounts or other contractual commitments with respect to the grants.

Off-balance Sheet Arrangements

The Company has not entered into any off-balance sheet arrangements. License agreements and operating leases are included in Contractual Obligations above, and foreign exchange derivative arrangements are described in Financial and Other Instruments below.

Transactions with Related Parties

The related party transactions are described in note 11 to the consolidated financial statements. There are no ongoing contractual or other commitments resulting from these transactions.

Fourth Quarter

Historically, the first and fourth fiscal quarters have the lowest levels of activity, corresponding to the seasonality of the installation of underground liquid storage systems in Canada. This seasonality is expected to continue, but may diminish as the Company expands its product lines into new markets that have different seasonality or that are less influenced by the effect of weather in the timing of installation.

In the fourth quarter, revenue was a record $10.4 million this year, up by 31.3% from $7.9 million last year. Net income for the fourth quarter increased to $1.2 million from $485,000 for the quarter last year. Basic earnings per share increased by $0.04, to $0.07 from $0.03 in 2004, and diluted earnings per share increased by $0.03, to $0.06 from $0.03 in 2004.

The increase in net income in the fourth quarter this year was largely due to the significantly higher revenue. As a result, revenue less manufacturing and selling costs increased to $2.6 million (25.4% of revenue) from $1.6 million in 2004 (20.3% of revenue). Amortization decreased in the fourth quarter this year, as the deferred costs related to the acquisition of the assets of ZCL-USA, Inc. were fully amortized. General and administration expenses increased by $155,000, from $467,000 in 2004 to $622,000 as a result of increased professional fees and accrual of management incentives in the fourth quarter this year. Financing charges decreased to $18,000 from $114,000 last year, as a result of the write-off of deferred finance costs in 2004. Income taxes were lower in the fourth quarter of 2004 with the recovery of prior years' taxes of $145,000.

Cash flows from operating activities decreased by $1.1 million, to $623,000 of cash used in operating activities from $471,000 cash flows from operating activities last year. This decrease was due to the timing of cash collections and payments during the quarter, as a high portion of sales were made late in the fourth quarter this year.

Outlook

To realize its vision, the Company must maintain its position in the Canadian marketplace, and pursue growth opportunities in related products and markets. Domestic and international markets for the Company's tank manufacturing and lining technologies will continue to be developed by leveraging customer relationships and innovative industry leadership. Continued success in reducing manufacturing costs and improving production processes will further enhance future profitability.

The Company's Prezerver system and other product innovations have a high level of industry acceptance. Utilizing proven technology and manufacturing expertise, a number of new products, such as the home heating oil aboveground tank, have been successfully introduced into several market sectors. The Company's product line has further been expanded through the acquisitions of Durex and Triple M.

The Company's home heating oil tank received UL approval for the USA market, and marketing activities commenced in the New England states, during the latter part of the year. A growing concern is the environmental and liability problems resulting from leaking tanks, and the Company's fiberglass products offer a new level of security for home owners, insurance companies and lenders. The North American home heating oil market represents an annual potential of 500,000 to 600,000 units or $400 to $500 million, and the Company's objective is to significantly increase its market share over the next five years.

Internationally, there is a very large and growing need for upgrading both underground and aboveground liquid storage, driven by environmental legislation and industry standards requiring secondary containment for storage of hazardous liquids. There are significant opportunities to establish ZCL's tank lining technologies as the preferred method of upgrading single wall tanks – the potential annual market in North America is estimated to be in excess of $300 million – and, at this time, there are no competitive alternative products in the marketplace. In conjunction with an alliance of major suppliers, the Company has developed and is testing new lining materials and processes that will provide superior quality and performance and inherently safe installation techniques. With the anticipated listing by ULC and UL, this new product is expected to add to revenue in fiscal 2006.

In May 2004, the Company acquired the business assets of Durex, a steel aboveground tank manufacturer. Aboveground storage systems are a significant portion of both the upstream (production) and downstream (retail) tank markets. This acquisition allowed the Company to access the aboveground retail market which is served only by steel products. Tank manufacturing and lining operations were expanded, and a full line of products are offered to existing alliance customers as well as to new customers.

Subsequent to March 31, 2005, the Company completed the purchase of 100% of the shares of Triple M, a manufacturer of fiberglass aboveground and underground tanks, vessels, pipe and other custom environmental products, located in Edmonton, Alberta. Triple M's specialized products and unique manufacturing expertise complement and enhance the Company's production capability and product line.

Certain upgrade and new installation programs in both sectors of the petroleum industry were deferred in prior years due to uncertainty and mergers and acquisitions. Activity in the downstream and upstream sectors of the petroleum industry, as well as other traditional markets, picked up in the latter part of fiscal 2003 and was strong throughout 2004 and 2005. With high commodity prices and the robust level of activity in the petroleum sector, many companies are continuing to forecast major capital expenditures for the coming year.

The Company also has international opportunities for its technology and manufacturing expertise. A global strategy will be implemented by developing joint ventures with local partners. In the USA marketplace, the Company is moving forward with tank lining and home heating oil tanks.

The Company is in a strong financial position and poised to grow both through internal expansion and acquisitions. While no further acquisitions are on the immediate horizon, a number of specific opportunities have been identified to complement the Company's core business and expand into new markets.

The Company's target continues to be to grow revenue by 15% to 20% on an annual basis, with a corresponding increase in net income. With continued strength in primary markets, and growth of new products, the Company believes this target is an achievable goal. Future growth will largely come from aboveground markets, including home heating oil tanks and expanded products with the acquisitions of Durex and Triple M, and tank lining systems, along with moderate continued growth in traditional underground markets. Actual growth each year will vary depending on economic and other conditions in various market sectors, and the Company's ongoing ability to deliver results and leverage its core competencies in technology, engineering and manufacturing.

The Company looks to growth in Canada, the USA and internationally, by utilizing its strong domestic base, customer alliances and industry leadership. Major oil companies are establishing global programs relating to procurement and standardization of specifications for their liquid storage systems, including the upgrade of existing tanks that otherwise may require costly replacement.

Risks and Uncertainties

In the normal course of business, the Company's operations are influenced by a number of internal and external factors, and exposed to risks and uncertainties, that can materially adversely affect its business, financial condition and operating results. In addition to the Risk and Uncertainties herein, the sections Critical Accounting Estimates and Financial and Other Instruments below, describe further risks and uncertainties related to the Company and its business.

Operations and Business Environment

The activities of the Company are subject to ongoing operational risks including the performance of key suppliers, product performance, proprietary technology and know-how, government and other industry regulations, successful integration of new acquisitions, dependence on key personnel, and reliance on information systems, all of which may affect the ability of the Company to meet its obligations. The ongoing ability to meet the needs of the marketplace is dependent on the development and introduction of new products and services. While management believes its innovation and technology make it a leader in the industry, revenue and results may be affected if products are not accepted in the marketplace, are not approved by regulatory authorities, or if products are not brought to market in a timely manner.

ZCL is engaged in competitive markets, subject to global economic and political influences and the financial strength of its customers. The Company is the leading manufacturer of fiberglass underground storage tanks in Canada, and its technology and products (high value-added complete liquid storage systems), operating structure, and professional customer service, differentiate it from its competitors. As a result of competition, demand for products could be reduced and revenue and margins may be adversely affected. The primary market for ZCL's products continues to be the Canadian petroleum industry; expanding into global markets, and other markets beyond the petroleum industry, will minimize the dependency on any particular industry or economic sector. If the Company cannot expand into global and other industry markets, the dependency on the Canadian petroleum industry will continue.

A number of factors, many of which are outside the control of the Company, may cause significant fluctuations in quarterly or annual revenue and operating results. Also, as the business is cyclical - historically, the second and third fiscal quarters have the highest levels of activity, corresponding to the seasonality of the installation of underground liquid storage systems in Canada – operating results will fluctuate from period to period. These fluctuations may negatively impact the business and prospects and, in turn, increase the volatility of the share price. Results from prior periods are not necessarily indicative of results for future periods.

Product Claims and Insurance

The Company manufactures and sells products that have a direct impact on the environment. Product failures could result in warranty and liability claims and the loss of customers. Correcting such failures or paying for such claims could require significant capital resources and have an adverse effect on operating results. The Company maintains high quality standards at its production facilities, uses only reputable suppliers for raw materials and other products, and has a history of no liability or warranty problems. ZCL also maintains insurance coverage for its assets and operations, including general liability, property, business interruption, boiler and machinery, automobile, directors and officers and other insurance. Each Prezerver liquid storage system carries a ten-year, insurance-backed warranty covering product replacement and $2 million of third-party pollution protection. There is no guarantee that insurance will sufficiently cover all potential claims, or that adequate or any insurance can be obtained or maintained. Liability or claims may also arise that cannot be insured or management may choose not to insure due to high premiums or for other reasons. With respect to the insurance claim relating to the electrical fire at the Waverley, Nova Scotia premises, there is no assurance that the entire claim for damages will be paid in full by the insurer.

Accounts Receivable and Credit Risk

The Company carries a high level of accounts receivable. Credit is spread among many customers and the Company has not experienced accounts receivable collection problems in the past. However, there is no assurance accounts receivable will be paid on a timely basis. Credit risk is described below and in note 16 to the consolidated financial statements. In addition, as described in note 12 to the consolidated financial statements, a provision for the full amount of the agreement receivable from Enviro was recorded during 2004.

Debt Availability and Interest Rate Risk

The Company requires ongoing working capital and financing to support operations and meet growth objectives. Long-term debt was repaid in full during 2004, and operating lines of credit are available but not utilized. While the Company has met all terms and covenants of these lending arrangements, there is no assurance that financing will continue to be available from this lender or alternative financial institutions on similar or any terms. In addition, the lines of credit bear interest at floating rates and when utilized, changes in interest rates would affect the amount of interest payable.

Foreign Exchange and Operations Risk

While the Company's operating results are reported in Canadian dollars, certain revenue and expenses are generated or incurred in other currencies, largely United States dollars and euros. Derivative financial instruments are used at times to manage a portion of the exposure to foreign exchange fluctuations. Substantially all business activities are currently carried out in Canada, but it is anticipated that exposure to, and fluctuation of, foreign currencies will be an ongoing risk in the future as the Company continues to expand into global markets.

Parabeam Industries BV, a wholly-owned subsidiary in The Netherlands, produces a three-dimensional fabric which is an intergral component of the Company's tank manufacturing and lining products. A small portion of the Company's third party business is also conducted through this integrated subsidiary. This business involves risks associated with foreign political and legal jurisdictions and foreign suppliers and customers. The translation of the revenue, expenses and balance sheet accounts of these foreign operations will impact the Company's operating results and financial position.

Disclosure Controls and Procedures

The Company's management, with the participation of the Chief Executive Officer ("CEO") and Chief Financial Officer ("CFO"), has evaluated the effectiveness, as at March 31, 2005, of the Company's disclosure controls and procedures (as defined in the Canadian Securities Administrators' proposed revised Multilateral Instrument 52-109, Certification of Disclosure in Issuer's Annual and Interim Filings). Based on this evaluation, the Company's CEO and CFO have concluded that such disclosure controls and procedures are effective in providing reasonable assurance that material information relating to the Company is made known to management in a timely manner.

Critical Accounting Estimates

The Company's financial statements have been prepared following Canadian generally accepted accounting principles ("GAAP"). The measurement of certain assets and liabilities is dependent upon future events whose outcome will not be fully known until future periods. Therefore the preparation of these financial statements requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues and expenses. Such estimates and assumptions have been made using careful judgments, which in management's opinion, are within reasonable limits of materiality and conform to the significant accounting policies summarized in the consolidated financial statements. Actual results may vary from those estimated.

Property, Plant and Equipment, Deferred Costs, Intangible Assets and Goodwill

Property, plant and equipment, deferred costs, and intangible assets with finite lives are recorded at cost less accumulated amortization. Goodwill and indefinite life intangible assets are recorded at cost. The unamortized balances, or carrying values, are regularly reviewed for recoverability or tested for impairment whenever events or circumstances indicate that these amounts exceed their fair values. The valuation of these assets is based on estimated future net cash flows, taking into account current and future industry and other conditions. An impairment loss would be recognized if the carrying value exceeds the fair value.

The acquisitions of business assets are accounted for using the purchase method and the allocation of the purchase price relating to the purchases is completed in accordance with GAAP in Canada. This allocation results in values being assigned to assets acquired based on expected future cash flows, and other methods, using estimates, assumptions and other information available at the time of acquisition.

Amortization of property, plant and equipment, deferred costs, and intangible assets with finite lives is based on estimates of the useful lives of the assets. The useful lives are estimated, and a method of amortization is selected, at the time the assets are initially acquired and then re-evaluated each reporting period.

Judgment is required to determine whether events or circumstances warrant a revision to the remaining periods of amortization. The estimates of cash flows used to assess the potential impairment of these assets are subject to measurement uncertainty. No impairment loss or write-down was required to be recognized in 2005 or 2004. A significant change in these estimates and judgments could result in a material change to amortization expense or impairment charges.

Warranties

The Company generally warrants its products for a period of one year after sale, and for up to thirty years for corrosion, if the products are properly installed and are used solely for storage of listed liquids. The Company's complete storage systems marketed under the Prezerver trademark carry a ten-year, insurance-backed warranty covering product replacement and $2 million of third-party pollution protection. The Prezerver warranty is covered by insurance underwritten by a major international insurer. A number of component materials and parts are similarly warranted by their manufacturers, thereby reducing the Company's exposure to warranty claims.

The Company provides for warranties based on a review of products and warranties taking into account the collective experience and history of the Company as to warranty claims on its products and other related factors. The Company maintains high quality standards at its production facilities, uses only reputable suppliers for raw materials and other products, and has a history of no liability or warranty problems. There is no guarantee that insurance will sufficiently cover all potential claims, or that adequate or any insurance can be obtained or maintained. The actual costs of warranties may vary from those estimated, and the difference may be material.

Allowance for Doubtful Accounts

The Company carries a high level of accounts receivable on its balance sheet. Credit is spread among many customers and the Company has not experienced accounts receivable collection problems in the past. The Company performs ongoing credit evaluations and maintains allowances for doubtful accounts, based on the assessment of individual customer receivable balances, credit information, past collection history and the overall financial strength of customers. A change in these factors could impact the estimated allowance and the provision for bad debts recorded in the accounts. The actual collection of accounts receivable and the resulting bad debts may differ from the estimated allowance for doubtful accounts and the difference may be material.

Impairment of Agreement Receivable

In fiscal 2004, a provision for impairment of the full amount of the agreement receivable from Enviro of $880,000 was recorded. As described in note 12 to the consolidated financial statements, Enviro had not made any payments under the agreement receivable since the fourth quarter of fiscal 2003, and due to current business conditions in the Philippines, had been unable to commit to a repayment schedule.

The provision for impairment was based on past experience, and the estimated amounts and timing of future repayment and the fair value of underlying security. Actions continue to be pursued to collect the balance of the receivable or otherwise realize upon security. Actual experience may result in the collection of the agreement receivable and the recovery of all, or a portion, of the provision for impairment.

Future Income Tax Assets

Future income tax assets are recognized for the benefits from tax losses and deductions when it is determined that it is more likely than not that the benefits will be realized. The Company considers such factors as the expected life of the losses, estimated future taxable income, and other characteristics and sources of realizing the benefits. A change in these factors could impact the estimated realization of the future income tax assets and the income tax expense of the Company. The majority of tax losses of prior years have been utilized by March 31, 2005, and current future tax assets largely represent the remaining tax losses that are available and anticipated to be utilized over the next year.

Financial and Other Instruments

The consolidated financial statements are reported in Canadian dollars, including the results of an integrated foreign subsidiary. Certain transactions, revenue and expenses are generated or incurred in other currencies, largely United States dollars and euros. The exchange rate risk, on an annual basis, primarily reflects the impact of fluctuating exchange rates on the net difference between revenue, expenses and other transactions in each of the currencies.

Derivative financial instruments have been used by the Company in the past to manage a portion of its exposure to foreign exchange rate fluctuations. The Company's policy is not to utilize derivative financial instruments for trading or speculative purposes.

In 2004, the Company entered into foreign currency forward contracts, options and collars to pay for certain raw materials denominated in euros, provided by a foreign subsidiary. These derivative contracts, not accounted for as hedges, were marked to market, and any changes in the market value were recorded in income or expense when the changes occurred. The fair values of these arrangements, estimated using market rates at March 31, 2004, was nil (March 31, 2005 - nil). During each of 2005 and 2004, net realized and unrealized gains of less than $5,000 relating to derivative financial instruments were recorded in financing charges.

Other

Additional Information

Additional information relating to the Company, including the Annual Information Form (AIF), is filed on SEDAR at www.sedar.com.

Outstanding Share Data

As at May 20, 2005, the following securities are outstanding:

	Number outstanding
Common shares	17,943,919
Share options	1,160,734
Warrants	3,445,878

Management Report

May 20, 2005

The Annual Report, including the consolidated financial statements, is the responsibility of the management of the Company. The consolidated financial statements were prepared by management in accordance with accounting principles generally accepted in Canada. When alternative accounting methods exist, management has chosen those it considers most appropriate in the circumstances. The significant accounting policies used are described in note 1 to the consolidated financial statements. The integrity of the information presented in the financial statements, including estimates and judgments relating to matters not concluded by year end, is the responsibility of management. Financial information presented elsewhere in this Annual Report has been prepared by management and is consistent with the information in the consolidated financial statements.

Management is responsible for the establishment and maintenance of systems of internal accounting and administrative controls which are designed to provide reasonable assurance that the financial information is accurate and reliable, and that the Company's assets are appropriately accounted for and adequately safeguarded.

The Board of Directors is responsible for ensuring that management fulfills its responsibilities and for final approval of the annual consolidated financial statements. The Board appoints an Audit Committee consisting of unrelated, non-management directors that meets at least four times each year under a written mandate from the Board. The Audit Committee meets with management and with the independent auditors to satisfy itself that they are properly discharging their responsibilities, reviews the consolidated financial statements and the Auditors' Report, including the quality of the accounting principles and significant judgements applied, and examines other auditing and accounting matters. The Committee approves the terms of the engagement of the auditors, reviews the annual audit plan and the results of the audit, and recommends to the Board the firm of auditors to be appointed by the shareholders.

The consolidated financial statements have been reviewed by the Audit Committee and approved by the Board of Directors of ZCL Composites Inc. The consolidated financial statements have been examined by the shareholders' auditors, Ernst & Young LLP, Chartered Accountants. The Auditors' Report outlines the nature of their examination and their opinion on the consolidated financial statements of the Company. The independent auditors have full and unrestricted access to the Audit Committee, with and without management being present.

Venence G. Côté
President and
Chief Executive Officer

Tony Barlott
Vice President Finance and
Chief Financial Officer

Auditors' Report

To the Shareholders of

ZCL Composites Inc.

We have audited the consolidated balance sheets of ZCL Composites Inc. as at March 31, 2005 and 2004 and the consolidated statements of retained earnings, income, and cash flows for the years then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of the Company as at March 31, 2005 and 2004 and the results of its operations and its cash flows for the years then ended in accordance with Canadian generally accepted accounting principles.

Ernst & Young LLP

Chartered Accountants

Edmonton, Canada
May 20, 2005

Consolidated Balance Sheets

As at March 31 (in thousands of dollars)	2005 $	2004 $
Assets		
Current		
Cash	**1,383**	1,880
Accounts receivable	**11,294**	6,363
Inventories *[note 3]*	**7,120**	5,556
Prepaid expenses	**548**	188
Future tax assets *[note 14]*	**250**	699
	20,595	14,686
Property, plant and equipment *[note 4]*	**8,246**	7,814
Deferred costs *[note 5]*	**707**	717
Intangible assets *[note 6]*	**1,085**	1,324
Goodwill	**1,991**	1,926
	32,624	26,467
Liabilities and Shareholders' Equity		
Current		
Accounts payable and accrued liabilities	**6,337**	4,525
Income taxes payable	**1,336**	35
Future tax liabilities *[note 14]*	**24**	27
	7,697	4,587
Government grants	**151**	160
Future tax liabilities *[note 14]*	**947**	838
	8,795	5,585
Commitments *[note 8]*		
Shareholders' equity		
Share capital *[note 9a]*	**19,277**	18,853
Contributed surplus *[note 9a]*	**171**	77
Retained Earnings	**4,381**	1,952
	23,829	20,882
	32,624	26,467

See accompanying notes

On behalf of the Board:

Venence G. Côté
Director

Jim Edwards
Director

Consolidated Statements of Retained Earnings

Years ended March 31 (in thousands of dollars)	2005 $	2004 $
Retained earnings (deficit), beginning of the year	**1,952**	(9,043)
Deficit elimination *[note 9a]*	**—**	9,043
Net income for the year	**3,480**	1,952
Dividends *[note 9b]*	**(1,051)**	—
Retained earnings, end of the year	**4,381**	1,952

See accompanying notes

Consolidated Statements of Income

Years ended March 31 (in thousands of dollars)	2005 $	2004 $
Revenue	**38,756**	33,932
Manufacturing and selling costs *[note 10a and 11]*	**29,669**	25,966
	9,087	7,966
Amortization *[notes 4, 5 and 6]*	**1,758**	1,968
General and administration *[note 10a]*	**2,029**	1,873
Provision for impairment of agreement receivable *[note 12]*	**—**	880
Financing charges *[note 13]*	**73**	370
Income before income taxes	**5,227**	2,875
Income taxes *[note 14]*		
Current	**1,192**	(42)
Future	**555**	965
	1,747	923
Net Income	**3,480**	1,952
Basic earnings per share *[note 15]*	**$0.20**	$0.11
Diluted earnings per share *[note 15]*	**$0.18**	$0.11

See accompanying notes

Consolidated Statements of Cash Flows

Years ended March 31 (in thousands of dollars)	2005 $	2004 $
Cash Flows from Operating Activities		
Cash receipts from customers	**33,782**	33,996
Cash paid to suppliers and employees	**(31,444)**	(27,714)
Interest paid	**(69)**	(176)
Income taxes recovered (paid)	**17**	(5)
	2,286	6,101
Cash Flows from Financing Activities		
Issue of common shares *[note 9a]*	**411**	—
Dividends *[note 9b]*	**(1,051)**	—
Repayment of long-term debt *[note 13]*	—	(4,643)
Repurchase of common shares for cancellation *[note 9a]*	—	(189)
	(640)	(4,832)
Cash Flows from Investing Activities		
Business acquisition *[note 2]*	**(1,193)**	—
Purchase of property, plant and equipment	**(432)**	(581)
Deferred development costs *[note 5]*	**(518)**	(141)
	(2,143)	(722)
Increase (decease) in cash	**(497)**	547
Cash, beginning of the year	**1,880**	1,333
Cash, end of the year	**1,383**	1,880

See accompanying notes

Notes to Consolidated Financial Statements

March 31, 2005 and 2004

1. Significant Accounting Policies

ZCL Composites Inc. (the "Company") manufactures and distributes liquid storage systems, including fiberglass underground and aboveground storage tanks and related products and accessories.

Generally accepted accounting principles

The Company's financial statements have been prepared following Canadian generally accepted accounting principles. The measurement of certain assets and liabilities is dependent upon future events whose outcome will not be fully known until future periods. Therefore the preparation of these financial statements requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues and expenses. Actual results may vary from those estimated.

In particular, the amounts recorded for amortization of property, plant and equipment, deferred costs and intangible assets are based on estimates of the remaining useful lives of such assets. Furthermore, the provision for warranty claims and the impairment of the agreement receivable are based on past experience and the most currently available information regarding warranty costs and the collectibility of the agreement receivable. These estimates, and those related to the cash flows used to assess the potential impairment of property, plant and equipment, deferred costs, intangible assets, and goodwill are subject to measurement uncertainty and the impact on the financial statements of future periods could be material. Such estimates and assumptions have been made using careful judgments, which in management's opinion, are within reasonable limits of materiality and conform to the significant accounting policies summarized below.

Effective April 1, 2003, the Company prospectively adopted the recommendation of the Canadian Institute of Chartered Accountants with respect to Handbook Section 1100, Generally Accepted Accounting Principles ("GAAP"). This standard establishes what constitutes Canadian generally accepted accounting standards and provides guidance on the GAAP hierarchy. The adoption of this standard had no effect on the Company's financial position, results of operations or cash flows.

March 31, 2005 and 2004

1. Significant Accounting Policies (continued)

Basis of presentation

The consolidated financial statements include the accounts of ZCL Composites Inc. and its wholly-owned subsidiary companies, LeGay Fiberglass (1993) Limited, Mocoat Services Incorporated, and Parabeam Industries BV (Netherlands). All significant intercompany transactions and balances have been eliminated in the preparation of these consolidated financial statements.

Inventories

Raw materials are valued at the lower of cost, determined on an average cost basis, and replacement cost. Work in progress and finished goods are valued at the lower of manufacturing cost and net realizable value on a specific item basis. Manufacturing cost includes the cost of raw material, direct labour costs, and applicable production overheads.

Property, plant and equipment

Property, plant and equipment are recorded at cost less accumulated amortization. Amortization is computed using the declining balance method at the following annual rates:

Buildings	4%
Land improvements	10%
Manufacturing equipment	10%
Office equipment	20%
Automotive equipment	30%

Amortization of leasehold improvements is computed using the straight-line method over the term of the lease.

Deferred development costs

The Company expenses research and development costs. Certain development costs are deferred when criteria established by the Canadian Institute of Chartered Accountants with respect to development costs are met, and amortized over future periods commencing with commercial production of the product or process.

Deferred development costs are amortized on a straight-line basis over the estimated expected life of the related products. All costs are currently being amortized over five years.

Unamortized deferred development costs are regularly reviewed for recoverability, based on projections of future revenues less relevant costs. The unamortized amount is written-off when the criteria for deferral are no longer met or written-down when the unamortized balance exceeds the amounts of deferred costs that can be reasonably regarded as recoverable.

Deferred start-up and finance costs

Deferred start-up and finance costs are recorded at cost less accumulated amortization. Amortization is computed using the straight-line method over the following periods:

Deferred start-up costs	5 years
Deferred finance costs	term of loan agreements

Deferred finance costs were amortized over periods ranging from three to five years.

March 31, 2005 and 2004

1. Significant Accounting Policies (continued)

Intangible assets

Intangible assets with finite lives are recorded at cost less accumulated amortization. Amortization is computed using the straight-line method over the following periods:

Licenses	term of licensing agreements
Non-patented technology	estimated expected life of related products
Non-contractual customer relationships	estimated expected minimum length of relationships

Licenses are amortized over periods ranging from eight to twenty years, non-patented technology over five years, and non-contractual customer relationships over three years.

Product certification and safety marks are indefinite life intangible assets recorded at cost and are not amortized.

Impairment of long-lived assets

Long-lived assets of the Company include property, plant and equipment, deferred start-up costs and intangible assets. These assets are tested for recoverability whenever events or changes in circumstances indicate that their carrying amount may not be recoverable. An impairment loss is then recognized when the carrying amounts exceed their fair value.

During the years, there were no events or changes in circumstances which indicated that the carrying amounts of long-lived assets may not be recoverable and no impairment loss was recognized.

Goodwill

Goodwill is recorded at cost. The carrying value is tested for impairment annually and when events or circumstances occur that would indicate that this amount may be impaired. An impairment loss would be recognized if the carrying value exceeds the fair value.

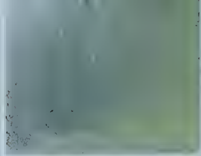
Warranties

The Company generally warrants its products for a period of one year after sale, and for up to thirty years for corrosion, if the products are properly installed and are used solely for storage of listed liquids. The Company's complete storage systems marketed under the Prezerver trademark carry a ten-year, insurance-backed warranty covering product replacement and $2 million of third-party pollution protection. The Prezerver warranty is covered by insurance underwritten by a major international insurer. A number of component materials and parts are similarly warranted by their manufacturers, thereby reducing the Company's exposure to warranty claims.

The Company provides for warranties based on a review of products and warranties taking into account the collective experience and history of the Company as to warranty claims on its products.

Government grants

Government grants relating to property, plant and equipment are recorded as a deferred credit and are amortized on the same basis as the property, plant and equipment to which they relate.



March 31, 2005 and 2004

1. Significant Accounting Policies (continued)

Derivative financial instruments

Derivative financial instruments are used by the Company to manage a portion of its exposure to foreign exchange rate fluctuations. The Company's policy is not to utilize derivative financial instruments for trading or speculative purposes.

The Company at times enters into foreign currency forward contracts, options and collars to pay for certain raw materials denominated in euros, provided by a foreign subsidiary. These derivative contracts, not accounted for as hedges, are marked to market, and any changes in the market value are recorded in income or expense when the changes occur. The fair value of these instruments is recorded as accounts receivable or payable.

Foreign currency translation

Transactions denominated in a foreign currency and financial statements of an integrated foreign subsidiary included in the consolidated financial statements are translated as follows: monetary items at the rate of exchange in effect at the balance sheet dates; non-monetary items at historical exchange rates; revenue and expense items at average exchange rates that produce substantially the same amounts that would have resulted had the transactions been translated on the dates they occurred; and amortization of assets at the same historical exchange rates as the assets to which they relate. Any resulting exchange gains or losses are included in income in the period incurred.

Revenue recognition

Revenue is recorded upon change of ownership, which normally occurs at the time of shipment of the product. In circumstances where the customer chooses to temporarily store goods on the Company's premises, revenue is recognized upon manufacturing completion.

Stock-based compensation

Direct awards of shares to employees and non-employees are accounted for in accordance with the fair value method of accounting for stock-based compensation. Effective April 1, 2003, the Company adopted the fair value method of accounting for share options granted and warrants transferred to employees and directors. The fair value of share options and warrants at the date of grant or transfer is determined using an option pricing model and compensation expense is recognized over the vesting period of the share options and warrants.

As permitted under the recommendations of the Canadian Institute of Chartered Accountants, this change was applied prospectively for new awards granted or modified on or after April 1, 2003. Pro-forma net income and earnings per share are disclosed for share options granted and warrants transferred in fiscal 2003 using the fair value method. For periods prior to April 1, 2002, the Company recognized no compensation expense when shares or share options were issued to employees and directors.

The Company's stock-based compensation, consisting of a share option plan and warrants, is more fully described in notes 9 and 10.

Income taxes

The Company uses the liability method to account for income taxes. Under this method, future income tax assets and liabilities are determined based on differences between financial reporting and tax bases of assets and liabilities, and measured using the substantively enacted tax rates and laws that will be in effect when the differences are expected to reverse.

Earnings per share

Basic earnings per share is computed based on the weighted average number of common shares outstanding during the year. Diluted earnings per share is computed using the treasury stock method, which assumes that the cash that would be received on the exercise of options and warrants is applied to purchase shares at the average price during the period and that the difference between the shares issued upon their exercise and the number of shares obtainable under this computation, on a weighted average basis, is added to the number of shares outstanding. Antidilutive amounts are not considered in computing diluted earnings per share.

March 31, 2005 and 2004

2. Business Acquisition

In May 2004, the Company acquired the business assets of Durex Steel & Alloy Industries Ltd. ("Durex"), located in Edmonton, Alberta. Durex manufactures steel aboveground storage tanks.

The acquisition was accounted for using the purchase method and the consolidated financial statements include the results of operations from May 7, 2004. Cash consideration for the purchase was $1,193,000, including acquisition costs. The fair value of assets acquired was as follows:

	2005
(in thousands of dollars)	$
Inventories	**128**
Property, plant and equipment	**800**
Non-contractual customer relationships	**50**
Product certification and safety marks	**150**
Goodwill	**65**
Total assets acquired	**1,193**

3. Inventories

	2005	2004
(in thousands of dollars)	$	$
Raw materials	**4,034**	2,685
Work in progress	**385**	236
Finished goods	**2,701**	2,635
	7,120	5,556

4. Property, Plant and Equipment

(in thousands of dollars)	2005 Cost $	2005 Accumulated amortization $	2004 Cost $	2004 Accumulated amortization $
Land	**293**	—	293	—
Buildings	**2,896**	**946**	2,876	865
Leasehold and land improvements	**311**	**108**	279	87
Manufacturing equipment	**11,352**	**6,142**	10,326	5,588
Office equipment	**1,559**	**1,029**	1,405	911
Automotive equipment	**165**	**105**	165	79
	16,576	**8,330**	15,344	7,530
Net book value	8,246		7,814	

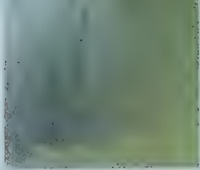
Amortization expense includes $800,000 (2004 - $748,000) for the amortization of property, plant and equipment and $9,000 (2004 - $9,000) for the amortization of government grants.

5. Deferred Costs

(in thousands of dollars)	2005 Cost $	2005 Accumulated amortization $	2004 Cost $	2004 Accumulated amortization $
Deferred development costs	**3,349**	**2,642**	2,831	2,114
Deferred start-up costs	**707**	**707**	707	707
Defered finance costs	**213**	**213**	213	213
	4,269	**3,562**	3,751	3,034
Net book value	707		717	

Deferred development costs include $518,000 (2004 - $141,000) incurred during the year. These costs relate to development projects in process at March 31, 2005 and were not amortized during the year. The total amount of research and development charged to expense for the year is not separately identifiable, as such costs are only tracked for development projects that are deferred.

Amortization expense includes $528,000 (2004 - $693,000) and $nil (2004 - $112,000) for the amortization of deferred development costs and deferred start-up costs respectively. Financing charges expense includes $nil (2004 - $198,000) for the amortization of deferred finance costs. In 2004, deferred finance costs were written-off as the related financing was repaid.



March 31, 2005 and 2004

6. Intangible Assets

(in thousands of dollars)	2005 Cost $	2005 Accumulated amortization $	2004 Cost $	2004 Accumulated amortization $
Intangible assets subject to amortization:				
Licenses	**521**	**431**	521	396
Non-patented technology	**1,944**	**1,134**	1,944	745
Non-contractual customer relationships	**50**	**15**	—	—
	2,515	**1,580**	2,465	1,141
Intangible assets not subject to amortization:				
Product certification and safety marks	**150**	—	—	—
	2,665	**1,580**	2,465	1,141
Net book value	**1,085**		1,324	

Amortization expense includes $35,000 (2004 - $35,000) for the amortization of licenses, $389,000 (2004 - $389,000) for non-patented technology, and $15,000 (2004 - $nil) for non-contractual customer relationships.

7. Bank Indebtedness

The Company has operating lines of credit of $10,250,000 provided by a chartered bank that are not utilized. These lines of credit are payable on demand and bear interest at prime rate plus 0.25% (4.50%; 2004 – 4.25%). The operating lines of credit contain certain restrictive covenants including the maintenance of certain financial ratios and limitations on capital expenditures and additional debt. The Company was in compliance with all covenants at March 31, 2005 and 2004. The Company has pledged as collateral a general security agreement, guarantees of subsidiaries, and a pledge of inventory under section 427 of the Bank Act.

8. Commitments

License agreements

The Company has license agreements which expire between October 2006 and December 2008. The agreements give the Company exclusive rights to manufacture and sell products in certain geographic areas utilizing the licensors' technology.

These license agreements provide for the payment of royalties based on revenues from related products during the license terms. Aggregate minimum royalty payments under these license agreements are as follows:

(in thousands of dollars)	$
2006	**467**
2007	**432**
2008	**380**
2009	**245**
	1,524

Operating leases

The minimum annual rentals under the terms of operating leases for premises and automotive and office equipment are as follows:

(in thousands of dollars)	$
2006	**407**
2007	**343**
2008	**238**
2009	**174**
2010	**174**
Thereafter	**329**
	1,665

March 31, 2005 and 2004

9. Share Capital and Contributed Surplus

a) Share capital and contributed surplus

Authorized

Unlimited number of common shares with no par or stated value

Issued and outstanding

	Share Capital				**Contributed Surplus**	
	2005		2004		**2005**	2004
(in thousands of dollars)	**Shares #**	**$**	Shares #	$	**$**	$
Balance, beginning of the year	**17,511,320**	**18,853**	17,716,920	27,378	**77**	745
Reduction of stated capital (i)	—	—	—	(8,298)	—	(745)
Share options exercised for cash	**194,266**	**185**	—	—	—	—
Warrants exercised for cash (ii)	**238,333**	**239**	—	—	**(13)**	—
Repurchased under normal course issuer bid (iii)	—	—	(222,000)	(240)	—	51
Issued to employees under employee recognition program (iv)	—	—	16,400	13	—	—
Stock-based compensation expense	—	—	—	—	**107**	26
Balance, end of the year	**17,943,919**	**19,277**	17,511,320	18,853	**171**	77

(i) At the Annual General and Special Meeting of Shareholders on August 18, 2003, the shareholders approved the reduction of the stated capital of the Company. Accordingly, in 2004, contributed surplus was reduced by $745,000, share capital by $8,298,000, and accumulated deficit by $9,043,000.

(ii) During the year, the amount credited to share capital related to the warrants exercised included $13,000 in respect of stock-based compensation expense previously included in contributed surplus.

(iii) During 2004, 222,000 common shares were repurchased for cancellation pursuant to a normal course issuer bid at a cost of $189,000. As a result, share capital was reduced by $240,000 and contributed surplus was increased by $51,000.

(iv) During 2004, 16,400 common shares were issued to employees as recognition for the Canada's 50 Best Managed Companies award received by the Company. As a result of this direct award of shares to employees, share capital and stock-based compensation expense (included in manufacturing and selling costs in the consolidated statements of income) of $13,000 were recorded.

b) Dividends

During the year, dividends in the amount of $1,051,000 ($0.06 per common share for all shareholders of record on July 14, 2004) were paid (2004 - nil).

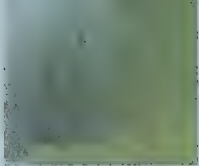
c) Share options

Under the Company's share option plan, options to purchase common shares may be granted by the Board of Directors to directors, officers, employees, and persons who provide management or consulting services to the Company. The plan has no cash or equity settlement features. As part of a private placement in September 2002, the Company agreed that the maximum term of opt ons would be no greater than five years, the exercise price would not be less than the price received by the Company upon the completion of the most recent offering of common shares, the total number of options would be no more than 10% of the issued and outstanding common shares, and the options would vest one-third per year, commencing on the first anniversary of the date the option is granted.

The shareholders authorized the number of options under the plan at 1,500,000 common shares. As part of the approval of the issue of the common shares under the employee recognition program in 2004, the Toronto Stock Exchange required that the number of options under the plan be reduced by 16,400, which was the number of common shares issued.

The Company has issued 1,160,734 (2004 - 1,145,000) of these options, which expire on dates between March 2006 and May 2009. The following table presents the changes during the years and the options outstanding:

	2005		2004	
	Shares	Weighted Average Exercise Price	Shares	Weighted Average Exercise Price
(in thousands of dollars)	#	$	#	$
Balance, beginning of the year	**1,145,000**	**0.97**	1,185,000	0.99
Granted	**260,000**	**1.40**	125,000	0.95
Exercised	**(194,266)**	**0.95**	—	—
Expired	**(50,000)**	**0.95**	(165,000)	1.05
Balance, end of the year	**1,160,734**	**1.07**	1,145,000	0.97



March 31, 2005 and 2004

9. Share Capital and Contributed Surplus (continued)

	2005			
	Options Outstanding		Options Exercisable	
Exercise Price	Shares	Weighted Average Remaining Contractual Like in Years	Shares	Weighted Average Exercise Price
$	#		#	$
0.95	830,734	2.62	562,156	0.95
1.35	70,000	0.93	70,000	1.35
1.40	260,000	4.15	—	—
0.95 - 1.40	1,160,734	2.86	632,156	0.99

d) Warrants

As part of a private placement in September 2002, the Company issued 3,684,211 Performance Warrants ("Warrant"). One-half of these Warrants were segregated, and approved by the shareholders at the Annual General and Special Meeting of Shareholders on August 18, 2003, for transfer to senior management of the Company. Each Warrant entitles the holder to subscribe for one common share at a price of $0.95 for a period of up to five years subject to a performance vesting provision. The Warrants vest at one-third intervals upon the weighted-average trading price of common shares reaching thresholds, for a period of twenty trading days, of $1.90, $2.85 and $3.80 per common share, of which the first two were reached in 2005.

During the year, 238,333 (2004 - nil) warrants were exercised.

10. Stock-Based Compensation

The Black-Scholes model, used by the Company to calculate the values of options and warrants, as well as other currently accepted option valuation models, were developed to estimate the fair value of freely-tradeable, fully-transferable options and warrants without vesting restrictions. Such options and warrants differ significantly from the share options granted and warrants transferred by the Company. These models require subjective assumptions, including future share price volatility and expected time until exercise, which affect the calculated values. Accordingly, management believes that these models do not necessarily provide a reliable single measure of the fair values of the share options granted and warrants transferred by the Company.

a) Share options granted and warrants transferred on or after April 1, 2003

The Company uses the fair value method of accounting for all share options granted and warrants transferred to employees on or after April 1, 2003. During the year, the Company granted 260,000 share options with exercise prices at the market share price on the grant date (2004 - granted 50,000 options with exercise prices in excess of the market price on the grant date), and transferred to employees 230,000 warrants with exercise prices below the market price on the transfer date (2004 - transferred 150,000 warrants with exercise prices in excess of the market price on the transfer date). Stock-based compensation expense of $98,000 (2004 - $10,000) was recorded in manufacturing and selling costs in the statements of income.

The following estimated fair values of these share options and warrants were determined, at the date of the grants or transfers, using the Black-Scholes option pricing model with the following weighted-average assumptions:

	Share Options		Warrants	
	Granted in Excess of Market	Granted at Market	Transferred in Excess of Market	Transferred Below Market
Weighted-average fair value	$0.29	$0.65	$0.18	$0.74
Risk-free interest rate (%)	3.89	3.77	4.37	3.77
Expected hold period to exercise (years)	4.0	4.0	4.5	3.3
Volatility in the price of the Company's shares (%)	60.8	55.5	60.5	51.4
Dividend yield (%)	0.00	0.00	0.00	0.00

During 2004, 75,000 share options were issued to a non-employee as consideration for consulting services. In accordance with the fair value method of accounting for stock-based compensation for non-employees, $9,000 (2004 - $16,000) was recorded as general and administration expense in the consolidated statements of income.

March 31, 2005 and 2004

10. Stock-Based Compensation (continued)

b) Share options granted and warrants transferred in fiscal 2003

The fair value of share options granted and warrants transferred in fiscal 2003, all of which were granted or transferred with exercise prices in excess of the market share price on the grant or transfer date, were determined, at the date of grants or transfers, using the Black-Scholes option pricing model. The following table provides the required pro-forma measures of net income and earnings per share had compensation expense been recognized based on the fair value, as at the date of the grant or transfer, of the options granted and warrants transferred to employees in 2003, in accordance with the fair value method of accounting for stock-based compensation:

(in thousands of dollars)	2005 $	2004 $
Net income for the year	**3,480**	1,952
Pro-forma adjustment for share options granted and warrants transferred in fiscal 2003	**207**	215
Pro-forma net income for the year	**3,273**	1,737
Earnings per share:		
Reported basic earnings per share	**0.20**	0.11
Pro-forma adjustment for share options granted and warrants transferred in fiscal 2003	**0.01**	0.01
Pro-forma basic earnings per share	**0.19**	0.10
Reported diluted earnings per share	**0.18**	0.11
Pro-forma adjustment for share options granted and warrants transferred in fiscal 2003	**0.01**	0.01
Pro-forma diluted earnings per share	**0.17**	0.10

The estimated fair values of these options and warrants were determined using the following weighted-average assumptions:

	Share Options	Warrants
Weighted-average fair value	**$0.37**	**$0.38**
Risk-free interest rate (%)	**4.0**	**4.0**
Expected hold period to exercise (years)	**4.0**	**5.0**
Volatility in the price of the Company's shares (%)	**61.6**	**56.2**
Dividend yield (%)	**0.0**	**0.0**

11. Related Party Transactions

Trucking services of $379,000 (2004 - $352,000), included in manufacturing and selling costs in the consolidated statements of income, were provided by a corporation controlled by a director of the Company. Accounts payable and accrued liabilities at March 31, 2005 included $6,000 (2004 - $6,000) owing to the corporation. Normal commercial rates were paid for these services.

12. Agreement Receivable

During 2004, a provision for impairment was recorded for the full amount of an agreement receivable of $880,000 from ZCL Enviro Systems, Inc. ("Enviro"), a Philippines corporation that manufactures products under a long-term licensing agreement utilizing the Company's technology. Enviro had not made any payments under the agreement since the fourth quarter of fiscal 2003, and due to current business conditions in the Philippines, had been unable to commit to a revised repayment schedule. The amounts and timing of future repayment, and the fair value of underlying security, net of expected costs of recovery, could not be estimated with reasonable reliability.

13. Financing Charges

(in thousands of dollars)	2005 $	2004 $
Interest, long-term	—	154
Interest, short-term	**51**	6
Foreign exchange losses	**22**	12
Amortization of deferred finance costs *[note 5]*	—	198
	73	370

Long-term debt in the amount of $4,643,000 was repaid in 2004.

March 31, 2005 and 2004

14. Income Taxes

The Company's effective income tax expense has been determined as follows:

(in thousands of dollars)	2005 $	2004 $
Statutory federal and provincial taxes	**1,700**	1,019
Increase (decrease) in income taxes resulting from:		
Recovery of prior years' taxes	—	(145)
Manufacturing and processing allowance	—	(33)
Impact of changes in tax rates	**(1)**	15
Non-deductible expenses and other items	**116**	67
Tax benefit of losses not previously recognized	**(68)**	—
	1,747	923

Significant components of the Company's future tax assets and liabilities are as follows:

(in thousands of dollars)	2005 $	2004 $
Future tax assets		
Loss carryforwards	**288**	739
Share issue costs	**72**	107
Tax basis of development costs in excess of carrying values	**507**	419
Other	**120**	196
	987	1,461
Future tax liabilities		
Carrying value of property, plant and equipment and intangible assets in excess of tax basis	**1,601**	1,566
Other	**107**	61
	1,708	1,627
	(721)	(166)
Represented by:		
Future tax assets - current	**250**	699
Future tax liabilities - current	**(24)**	(27)
Future tax liabilities - long-term	**(947)**	(838)
	(721)	(166)

The Company has accumulated losses for Canadian tax purposes of approximately $770,000 which may be carried forward and used to reduce taxable income in future years.

The Canadian tax losses available for carryforward must be claimed in years ending no later than:

(in thousands of dollars)		$
	2009	**91**
	2010	**449**
	2012	**230**

The potential income tax benefit associated with these losses has been recognized for accounting purposes.

15. Earnings Per Share

The following table sets forth the net income available to common shareholders and weighted-average number of common shares outstanding for the computation of basic and diluted earnings per share:

(in thousands of dollars, except number of shares)	**2005** $	**2004** $
Numerator:		
Net income available to common shareholders	**3,480**	1,952
Denominator:		
Weighted-average shares outstanding - basic	**17,686,512**	17,640,106
Effect of dilutive securities		
Share options	**597,894**	48,041
Warrants	**997,537**	—
Weighted-average shares outstanding - diluted	**19,281,943**	17,688,147

In 2005, certain of the warrants were not included in the calculation of diluted shares as the market price was below the performance vesting thresholds. In 2004, certain share options were not included in the calculation of diluted shares as their exercise prices exceeded the average market share price, and the warrants were not included as the market price was below the performance vesting thresholds.

March 31, 2005 and 2004

16. Financial Instruments and Risk Management

Financial instruments

The fair value of accounts receivable, accounts payable and income taxes payable approximate their carrying values, due to the relatively short periods to maturity of these instruments.

Foreign currency risk management

The consolidated financial statements are reported in Canadian dollars, including the results of an integrated foreign subsidiary. Certain transactions, revenue and expenses are generated or incurred in other currencies, largely United States dollars and euros. The exchange rate risk, on an annual basis, primarily reflects the impact of fluctuating exchange rates on the net difference between revenue, expenses and other transactions in each of the currencies. Substantially all business activities are currently carried out in Canada, but it is anticipated that this will be a continuing risk in the future as the Company continues to expand into global markets.

Interest rate risk management

All long-term debt was repaid during 2004, and available lines of credit are not utilized. The lines of credit bear interest at floating rates, and if utilized, changes in interest rates would effect the amount of interest payable.

Credit risk management

The maximum exposure to credit risk is represented by the carrying amount of the accounts receivable. A provision for impairment of the full amount of an agreement receivable was recorded in 2004 as described in note 12. The credit risk related to accounts receivable results from the possibility of customers defaulting on payment of these accounts. The Company deals largely with major oil and gas companies in Canada, and performs ongoing credit evaluations and maintains allowances for potential doubtful accounts. No one customer generally makes up more than 10% of revenue, but at a particular point in time, depending on the timing of sales, there may be higher proportionate exposure in accounts receivable. At March 31, 2005, two customers accounted for 22% (2004 - two customer, 26%) of accounts receivable.

17. Segmented Information

Operating segments are defined as components of the Company for which separate financial information is available that is evaluated regularly by the chief operating decision maker in allocating resources and assessing performance. The chief operating decision maker of the Company is the Chief Executive Officer.

The Company operates in one reportable segment, which is the manufacture and distribution of liquid storage systems including fiberglass underground and aboveground storage tanks and related products and accessories.

Information about products

Providing information relating to revenue from external customers for each product, or group of similar products, is impractical and accordingly, only total revenue has been presented in the statements of income.

Information about geographic areas

	Revenues		Property, plant and equipment and goodwill	
	2005	2004	2005	2004
(in thousands of dollars)	$	$	$	$
Canada	**36,930**	32,436	**9,504**	8,934
Foriegn countries	**1,826**	1,496	**733**	806
	38,756	33,932	**10,237**	9,740

Revenue is attributed to the geographic area based on location of the Company's operations. No revenue attributed to any individual foreign country is material. The property, plant and equipment relating to foreign countries are located in The Netherlands.

Information about major customers

The Company has long-term contracts and alliance arrangements with many of the major oil and gas companies in Canada. The top seven customers (same seven in 2004) accounted for approximately 41% (2004 - 38%) of revenue, with the largest customer making up 10% (2004 - 11%) of revenue.

March 31, 2005 and 2004

18. Subsequent Events

a) ZCL Composites Inc. and its wholly-owned subsidiaries LeGay Fiberglass (1993) Limited and Mocoat Services Incorporated were amalgamated under the name ZCL Composites Inc. on April 1, 2005.

b) Subsequent to March 31, 2005, the Company acquired 100% of the shares of Triple M Fiberglass Mfg. Ltd. ("Triple M"). Triple M, located in Edmonton, Alberta, manufactures fiberglass aboveground and underground tanks, vessels, pipe and other custom environmental products. The total purchase price, subject to final adjustments, of approximately $1,900,000 was paid in cash on closing.

19. Comparative Figures

Certain comparative figures have been restated, where necessary, to conform with the current year presentation.

Corporate Information

Board of Directors
James S. Edwards, Chairman of the Board
Venence G. Côté, Director, President and CEO
Fred J. Dyment, Director
Nancy L. Smith, Director
Simon Sochatsky, Director

Annual General Meeting
1:00 pm on Monday, August 15th, 2005
at The Westin Edmonton
10135 - 100 Street, Edmonton, Alberta

Corporate Office
6907 - 36 Street
Edmonton, Alberta
Canada T6B 2Z6

Common Shares Outstanding
as of May 20, 2005
Total Outstanding: 17,943,919

Investor Relations
Copies of this Annual Report
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Tony Barlott at 780-466-6648
or email tony.barlott@zcl.com

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T2G 0P6

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Scotia Place
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Edmonton, Alberta
T5J 3R8

General Counsel
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Edmonton, Alberta
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Stock Listing and Share Symbol
Toronto Stock Exchange: **ZCL**

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